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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: OCT 1 1999

Contact Person:

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Ladies and Gentlemen:

This is in reply to a letter dated June 22, 1999, from your legal representative in which she requested rulings concerning the income tax consequences of certain transactions arising from a recent corporate reorganization.

B was created to specifically act as the parent in the system to provide administrative services to C, D, E and F. The services that were formerly provided to C and D by employees of both will be provided by B. Any employees providing shared administrative services will be transferred to B. Thus, B's role is provide services to C, D, E and F and to ensure that they operate in a manner consistent with the best interests of the system as a whole. B will also interact with outside agencies interested in programs undertaken by C, D, E and F.

The reorganization is intended to transfer administrative staff to B so that B may focus on administration of the system and the operational entities may dedicate themselves exclusively to the services being provided. In its role as parent, B will monitor and guide the activities of C, D, E and F to ensure that all components of the resulting system work together in a complementary manner to reduce functional overlaps and maximize the utilization of available resources.

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B was created at the request of many of C's and D's funders. Because the organizations had similar administation, shared facilities, and similar, though different, goals, the funders thought it would be best to have an entity ensuring that the operation of C and D were coordinated in all ways, and that they were not competing with each other for resources. The Boards of Directors of C, D, E and F agreed because they had often acted in concert and believed that it would be in the best interests of C, D, E and F. The reorganization of C, D, E and F entailed the creation of B, which is the sole member of C, D, E and F. C, D, E and F then became, in effect, subsidiaries of B.

The reorganization also entailed the amendment of C, D, E and F's governing documents to provide that B will be the sole member of each entity and to reserve certain powers to B as member. The amendments are intended to provide B with sufficient control and authority to ensure that the system operates as one exempt unit. B has the authority to act as the parent in the system, with C, D, E and F as subsidiaries. Thus, as a result of the reorganization, the system is subject to common control, and B has authority to ensure integration of activities of C, D, E and F.

We have determined that B is tax-exempt under section 501(c)(3) and other than a private foundation under section 509(a)(3) of the Code in separate correspondence.

C is an exempt educational organization described in section 501(c)(3) and classified as other than a private foundation under sections 509(a)(a) and 170(b)(1)(A)(ii) of the Code. The purpose of C is two-fold: (1) to provide high quality arts education programming to minority, inner city youth; and (2) to assist emerging and established professional artists to further their careers, visibility, and professional standing.

D is an exempt post-secondary educational organization desribed in section 501(c)(3) and classified as other than a private foundation under sections 509(a)(1) and 170(b)(1)(A)(ii) of the Code. The primary objective of D is to provide remedial, basic readjustment, and occupational skill training to the unemployed, disadvantaged, and dislocated worker population in southeastern G.

E is an exempt organization described in section 501(c)(3) and classified as other than a private foundation under section 509(a)(3) of the Code. E's purpose is to undertake fundraising on behalf of C and D. E solicits potential funders for contributions to build an endowment for both C and D.

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F is an exempt organization described in section 501(c)(3) and classified as other than a private foundation under section 509(a)(3) of the Code. F's purpose is to create an incubator in a facility so that there would be economic development and employment opportunities in the area around C and D.

B has represented that C, D, E and F will continue to operate in accordance with their previously stated exempt purposes; that B will operate as represented herein and in its Form 1023 application; that the reorganization was undertaken to facilitate the long-term viability of C, D, E, and F by permitting one Board of Directors to make decisions as to the best course for the system as a whole. The separate Boards of Directors for C, D, E and F will continue to operate in a manner they believe to be in the best interests of C, D, E and F, respectively.

B has further represented that it will be reimbursed by C, D, E and F for the costs of administrative services provided to C, D, E and F. B does not anticipate receiving excess funding.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of an organization organized and operated exclusively for educational and charitable purposes.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of the other tax-exempt purposes which may fall within the broad outlines of "charity" as developed by judicial decisions.

Section 511 of the Code imposes a tax on the unrelated business taxable income of organizations described in section 501(c)(3).

Section 512(a)(1) of the Code defines unrelated business taxable income generally as gross income received by an exempt organization from an unrelated trade or business regularly carried on by it, less allowable deductions.

Section 513(a) of the Code defines an unrelated trade or business, in the case of any organization subject to the tax imposed by Section 511, as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the

profits derived) to the exercise or performance by such organization of its exempt purpose.

Section 509(a) of the Code provides that a section 501(c)(3) organization shall be a private foundation unless it is described in sections 509(a)(1) through 509(a)(4).

Section 509(a)(3)(A) of the Code describes an organization that is organized and operated exclusively to support or benefit one or more specified section 509(a)(1) or (2) organizations which have a degree of control or supervision over the supporting organization.

Section 1.509(a)-4(c)(1) of the regulations provides that an organization is organized exclusively for one or more of the purposes specified in section 509(a)(3)(A) only if its articles of organization:

(i) Limit the purposes of such organization to one or more of the purposes set forth in section 509(a)(3)(A);

(ii) Do not expressly empower the organization to engage in activities which are not in furtherance of the purposes referred to in subdivision (i) of this subparagraph;

(iii) State the specified publicly supported organizations on whose behalf such organization is to be operated (within the meaning of paragraph (d) of this section); and

(iv) Do not expressly empower the organization to operate to support or benefit any organization other than the specified publicly supported organizations referred to in subdivision (iii) of this subparagraph.

Section 1.509(a)-4(e)(1) of the regulations provides in part that a supporting organization "will be regarded as 'operated exclusively' to support one or more specified publicly supported organizations (herein after referred to as the 'operational test') only if it engages solely in activities which support or benefit the specified or publicly supported organizations."

Section 509(a)(3)(B) of the Code sets forth three different types of relationships, one of which must be met in order for a Section 501(c)(3) organization to qualify under the provisions of Section 509(a)(3). A supporting organization may be:

1. operated, supervised, or controlled by,

2. supervised or controlled in connection with, or

3. operated in connection with, one or more publicly supported organizations.

Section 1.509(a)-4(i)(1) of the regulations provides that an organization is "operated in connection with" a publicly supported organization if it satisfies a "responsiveness test" and an "integral part test." The responsiveness test is satisfied if one or more of the trustees of the publicly supported organization are also trustees of, or hold important offices in, the supporting organization. The integral part test is satisfied if the activities engaged in by the organization for or on behalf of the supported organization are activities to perform the functions of, or to carry out the purposes of the supported organization and, but for the supporting organization, such activities would normally be performed by the supported organization.

Section 509(a)(3)(c) of the Code excludes from the definition of private foundations an organization which is not controlled directly or indirectly by one or more disqualified persons (as defined in section 4946) other than foundation managers and other than one or more organizations described in paragraph (1) or (2).

The facts and circumstances of this case indicate that the recent reorganization will not adversely affect the tax-exempt or nonprivate foundation status of B, C, D, E or F in that B, C, D, E and F will continue to provide services in furtherance of their exempt purposes. There will be no changes in funding sources or in the relationships among the entities.

The facts and circumstances further indicate that the transfer of assets and the provision of services among B, C, D, E and F serve to facilitate their exempt activities and promote the achievement of the exempt purposes of each related organization. Therefore, these transactions do not adversely affect the exempt status of B, C, D, E or F.

Moreover, since B controls C, D, E and F, the payments made by C, D, E and F to B for services rendered do not generate unrelated business trade or business income; and, C, D, E, and F may transfer assets to B and each other without generating unrelated trade or business income since the transfer would be merely a matter of accounting.

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To the extent that income is realized as a result of the sharing of assets and services among B, C, D, E and F, it will not give rise to unrelated business income so long as these business activities are substantially related to the exercise and performance of the exempt purposes of B, C, D, E and F.

Accordingly, based on the facts and circumstances as stated above, we rule that:

1. The reorganization will not adversely affect the tax-exempt or nonprivate foundation status of B, C, D, E or F.

2. Any sharing or transfers of funds, assets, services, and/or personnel by or among B and C, D, E and F will not jeopardize the tax-exempt or nonprivate foundation status of B or C, D, E or F or generate unrelated business income taxable under section 511.

This ruling is based on the understanding that there will be no material changes in facts upon which it is based.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited by others as precedent.

We are informing your key District Director of this action. Please keep a copy of this ruling in your permanent records.

Sincerely yours,

Gerald V. Sack

Gerald V. Sack
Chief, Exempt Organizations
Technical Branch 4